RICHARD RUSSELL'S **DOW THEORY LETTERS, INC.**

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May 5, 1982 **LETTER 834**

Apr. 23, DJIA 862.16; PTI 1391; A-D Ratio –23.88
Apr. 30, DJIA 843.36; PTI 1387; A-D Ratio –24.25

THE MARKET: We returned from New York last night. I waded through about 30 pounds of mail, up-dated those charts that I didn't take with me–and now it's back to the desk. I really don't know how this Letter is going to come out or whether it will be abbreviated. I'm writing this at 4AM, and I'll just have to see where the typewriter takes me.

As you can see on the chart below, the advance took the D-J Industrial Average from 795.47 (March 8) to 865.58 (April26). That's roughly 70 points in 7 weeks–which qualifies as a decent correction of the drop from the December high (892.69). Moreover, the correction has already turned a lot of people bullish, and the institutions and pension funds have been buying their heads off (we know they have from the position of the big block index and the new peak in the positive volume index).

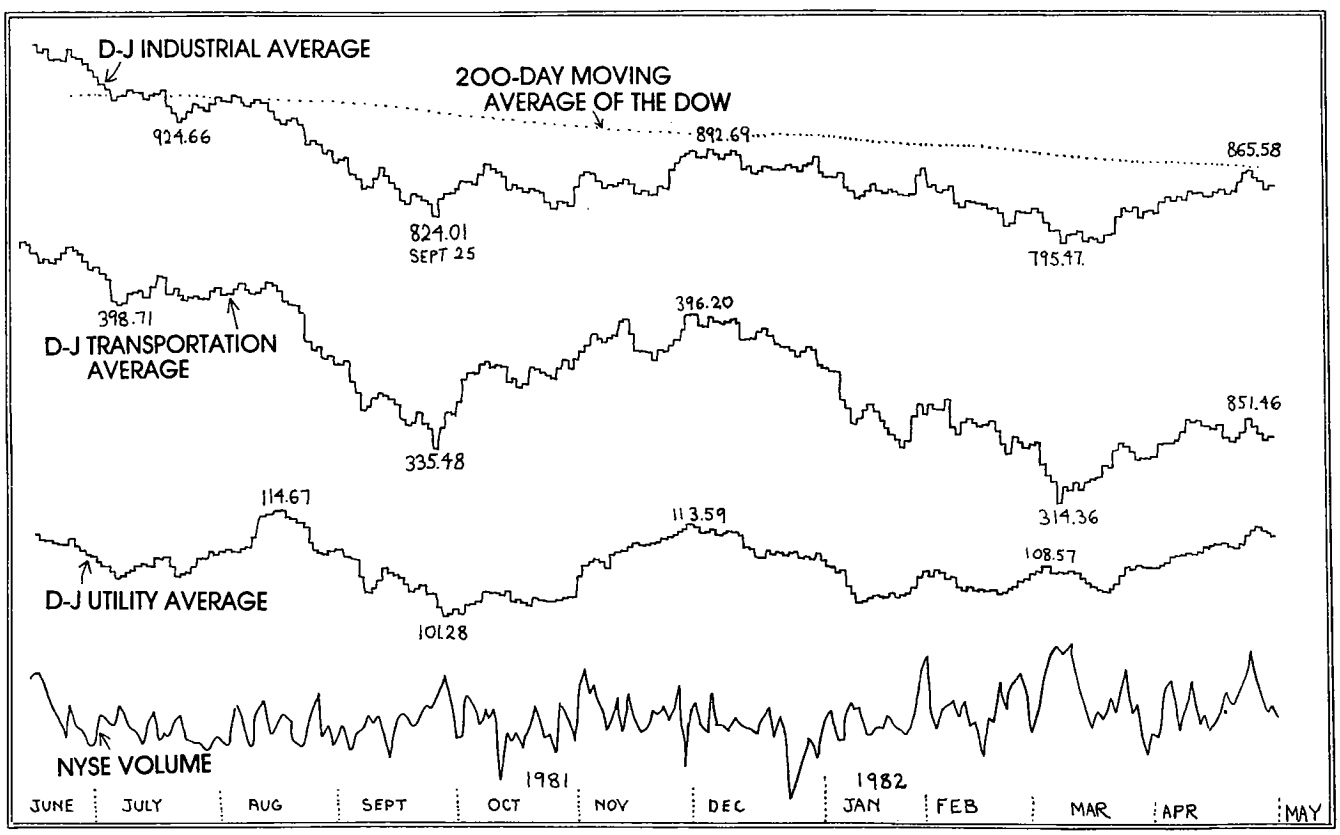
Very few market rallies just hit a peak and die. There's usually a dip, then a second attempt at a new high. Therefore, it won't surprise me at all if the Dow tries to better 868.58 and the Transports try to better 35146. If they do hurdle those points the rally could extend–maybe into May or even June. But if one or both Averages fail to better the April 26 highs, then the bear's going to survey the whole scene–and he's almost sure to attack again.

Remember (as I wrote in Letter 833) "The bear's fondest desire is to take as many stockholders as he can with him–when he makes his next trip to lower levels." To do this he must offer hope, he must foster greed, he must allow the market to appear enticing." So far, I think the bear's done a pretty good job of it. Bullishness has been rising with the market, and many analysts are talking about "a new bull market." Others are saying that "we could hit Dow 1000 by summer."

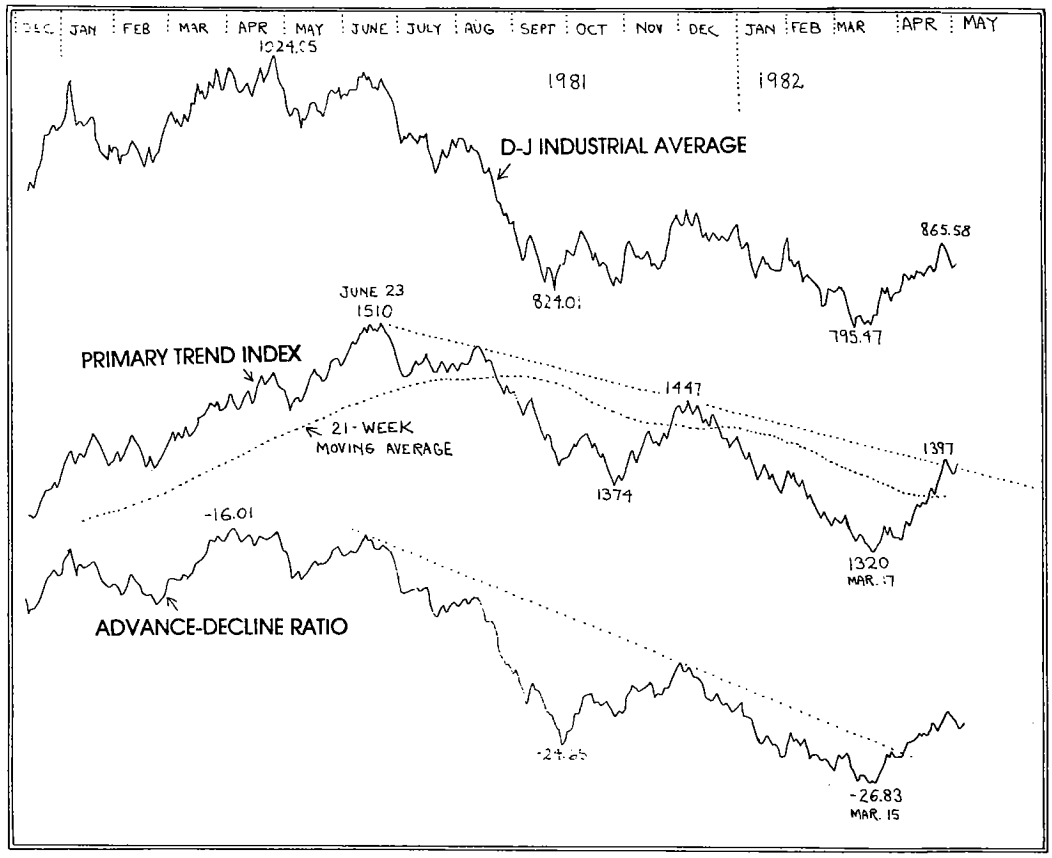
When you think about it, the change on Wall Street and Main Street has been little short of amazing. Mid-March and most observers were talking "bear market and trouble." Less than two months later, here in early-May, many of these same experts are hailing the birth of a new bull market. Wall Street, like the proverbial woman, is entitled to change its mind.

FRONT PAGE COMMENT: Will the budget "problem" be solved? How will it be solved? Well, it won't be solved in 1982. As I've said so many times before, politicians don't move until events force them against the wall. This nation is not in a depression. The markets aren't crashing. Interest rates aren't at 20%. So the President and Congress will play games, jockey for position, and maybe Congress will finally come up with some kind of mish-mash, and they'll call it a compromise. It won't begin to address the problems of a budget that's going completely out-of-control, but Congress will say "that it's the best they can do in a tough election year," and the debts and deficits will continue to build.

And the bear will laugh to himself, because he'll know that the big pain has simply been put off for a while–but just a while. And the bear will repeat to himself Puck's famous line, "What fools these mortals be."

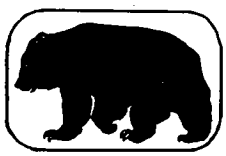


Ah, but there's a catch. Sentiment was never terribly bearish at the March lows. The institutions never stopped buying at the March lows. And bullishness blossomed far too quickly by mid-April. If March saw a bear market bottom, that bottom was different than any this observer has ever witnessed.

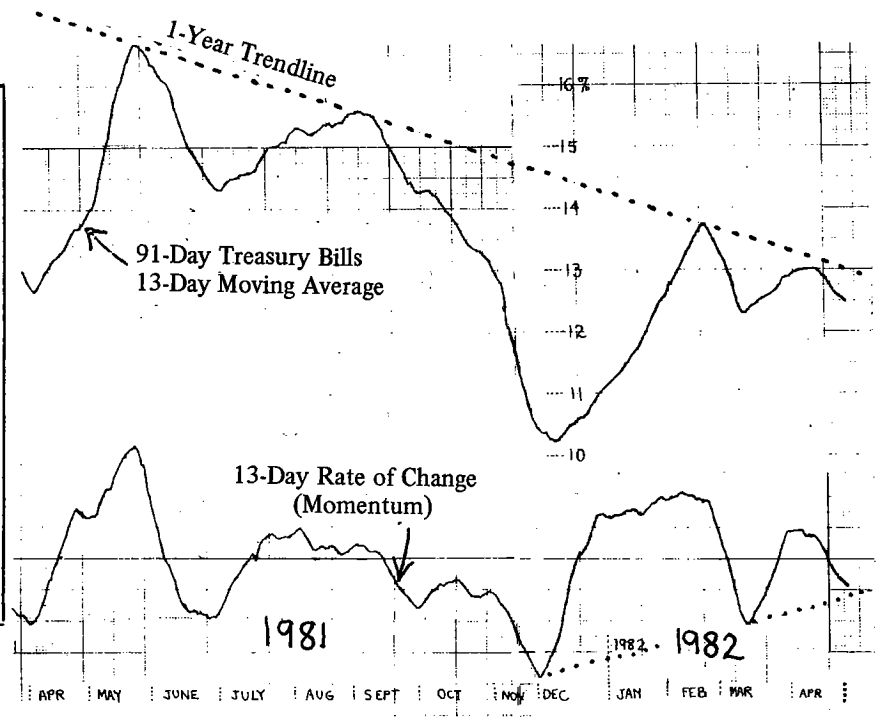


Turning to the Primary Trend Index (PTI), note that it rallied to 1397 on April 26, well above its 21-week moving average—and yes, right to its declining trendline (a trendline connecting the July and December peaks). From the standpoint of the PTI, I want to see whether this index can construct a new bullish pattern, or whether the rally is simply part of a major overall downtrend. We've got to be absolutely impartial as far as the PTI is concerned. It's going to tell us what's going on, we're not going to tell the PTI. And it's going to take a while to see what we have here. Luckily, we're in no hurry. We've got plenty of time.

INVESTMENT POSITION: Our major position continues to be 91-day Treasury bills. But I've allowed for initial positions in long-term bonds. I said that 10% to 20% of your money in long-term Treasury bonds is all right, and the same kind of position in 2 to 4 year notes is OK. There's no big risk in either case.



But I'm more interested in keeping subscribers liquid, and I mean short-term liquid. So think in terms of CASH, and think in terms of liquidity and you'll be in good shape. There's been a lot of money lost so far in trying to beat this bear market. And I expect to see many billions more lost—before this bull breathes its last.



MONEY: Just about every analyst in the nation has predicted a collapse in interest rates. But it hasn't happened yet. Rates have come down a bit, but they stay generally high. The 91-day bills hold above the 12% level like a bull terrier hanging on to a bone.

This chart shows the 13-day moving average of the 91-day bill yields (I use the daily bid price). It also shows the 13-day rate-of-change for the bills. But what interests me here is that the bill yield (upper line) has been holding below a declining trendline for a year. That's a long time for a 91-day bill trendline. Note that the trendline has been tested four times, so we know it's a valid trendline. Note also that the bills are now holding just under the trendline.

All of which leads me to wonder what would happen if the bills were to push above that one-year trendline (it would take a yield of about 13% to break the trendline to the upside). If the bills were to reverse that trendline, we could have an upside explos-

ion in yields. That would come as a shock to everyone–everyone, that is but readers of these reports. I think it could happen. That trendline is getting old, and the rate-of-change (lower line) could be ready to turn up.

QUESTIONS & ANSWERS: Question: How safe are my Treasury bills in a bank or in a brokerage office?

Answer: According to the Fed's legal dept, member banks may not co-mingle T-bills held for customers with their own assets. This is not true for brokers (as I found out when I called the New York Fed). However, most of the major brokers are in better shape than the banks. At this time, I don't see any problem with holding T-bills at outfits like Merrill, Lynch, EF Hutton, Dean Witter Sears. Remember, most of the brokerage houses have seen wild ups and downs over the past five years, and they have grown quite sophisticated about surviving in a roller-coaster economy. Unless, things get much worse (and we should be able to spot this), I would not worry about holding T-bills in the major brokerage houses.

Question: What do you think of zero-based bonds?

Answer: Not much. A zero based bond sells at a discounted basis with no interest until maturity. Thus, the bond pays a "guaranteed" rate of interest in that you can figure out your final return and your average interest rate. But my objection to the zero based bonds is two fold: (1) With a regular bond you are getting protection by accumulating interest. For instance, with a bond paying 15% you have half your investment back in three years. Not so with the zero-based bond where you risk everything for a full redemption at maturity. (2) I object to corporations taking in money without having to pay out interest year after year. A corporation can take in millions via zero-based bonds, then have to face the full brunt of the redemption years from now. The zero-based bond is the ultimate "grab it now, pay it later" concept–with the buyer taking the risk.

Question: Russell, it seems to me that you have taken a very conservative or safe stance towards investing ever since April of 1981. How is it that you haven't recommended more trading plays?

Answer: There are a lot of trading services. In fact, most of the brokerage houses will be only too happy to provide you with trading "advice." Over the past 25 years I've seen trading services come and go–hundreds of them. "But why," you ask, "why do they come and go?" And the answer is that the great majority of trading services lose money for their clients. The money comes and goes: it comes to the trading services and goes with the readers' trading. And then the readers go as well.

To my mind, with interest rates at double digit, the only phenomena which would justify major stock positions are (1) a new primary bull market, (2) a crash, since a panic-crash is always followed by a rebound which recovers at least half of the crash losses. Barring these two contingencies, trading in a difficult and emotional market such as this one is simply an exercise in "equity crap-shooting."

Just as 1949 and 1962 and 1970 and 1974 provided great opportunities for investing in equities, the early 1980's are providing great opportunities for safe compounding of capital at historically high interest rates. The art of investing entails a fundamental knowledge of VALUES. If you don't understand this concept, you are on your way to losing your money in the markets.

NEW YORK: We left San Diego on the "red eye." taking off at 9PM and arriving in the City at 6AM. Why the red eye? I like night flying, and I like getting to NYC very early–before traffic stops up the City like a giant cork.

I have a love-hate relationship with NYC. I love it because I grew up in Manhattan; it's my first home. And I love it because it's the most exciting city in the world. I love it because it's got MORE of everything than any other city (except breathing space), and I love it because it's beautiful the way a battered Tiger tank or King Kong is beautiful. But I hate New York because it drives everybody slightly (or in some cases totally) crazy. It's too crowded, too greedy, too dirty, too expensive, too tough, too devoid of grass and parks and sitting space. And NYC is status-happy. In NY status and money rule, and if you haven't got one or both you had better be very philosophical.

We stayed at the Mayfair Regent because Esquire Mag said that it was the "best" smaller hotel in the City, and we wanted to try it. I believe they're right. We also freaked out on the BEST food in the nation including the Four Seasons and (courtesy of my old buddy, Jay Pack) Le Cirque and Cote Basque. Friends Peter and Elga Gimbel took us to the inner sanctum (main room of the famous "21"). People-watching at 21 puts Hollywood and Vine to shame. As for NYC food, it is without doubt the very best (and don't tell me about LA and SF, we've tried them).

For four days I jog along what I consider the world's most interesting jogging path–Fifth Avenue. I do it at 6AM, and it's always (for me) a thrill to pass Bonwit's and GM Plaza and Bergdorf's and the Pierre on a cool morning in a traffic-less NYC with only a few cops, a few vagrants and maybe a doorman or two around. I do the only thing that will surprise a NY cop, I say "good morning" as I jog past. They nod, looking puzzled. "This nut must be from out of town." But I'm having fun, and I stop to catch my breath and study the book display at Doubleday.

My beautiful wife, Paula, has a strange habit. She keeps running (inadvertently) into celebrities. In Honolulu she met Goldie Hawn on the beach and my kids and Miss Hawn's kids played together since they couldn't care less who mommy is. This time, while at a NY jazzercise class, Paula got friendly with a gal who turned out to be Marlo Thomas. Marlo dropped Paula off at the hotel, and let's face it, Paula had a good time. Later Paula met Cindie Garvey in a shoe store (how come it never happens to me?). Quoth Paula, "It takes jazzercize to offset great food, so with any luck my body will stay at status quo"). It did.

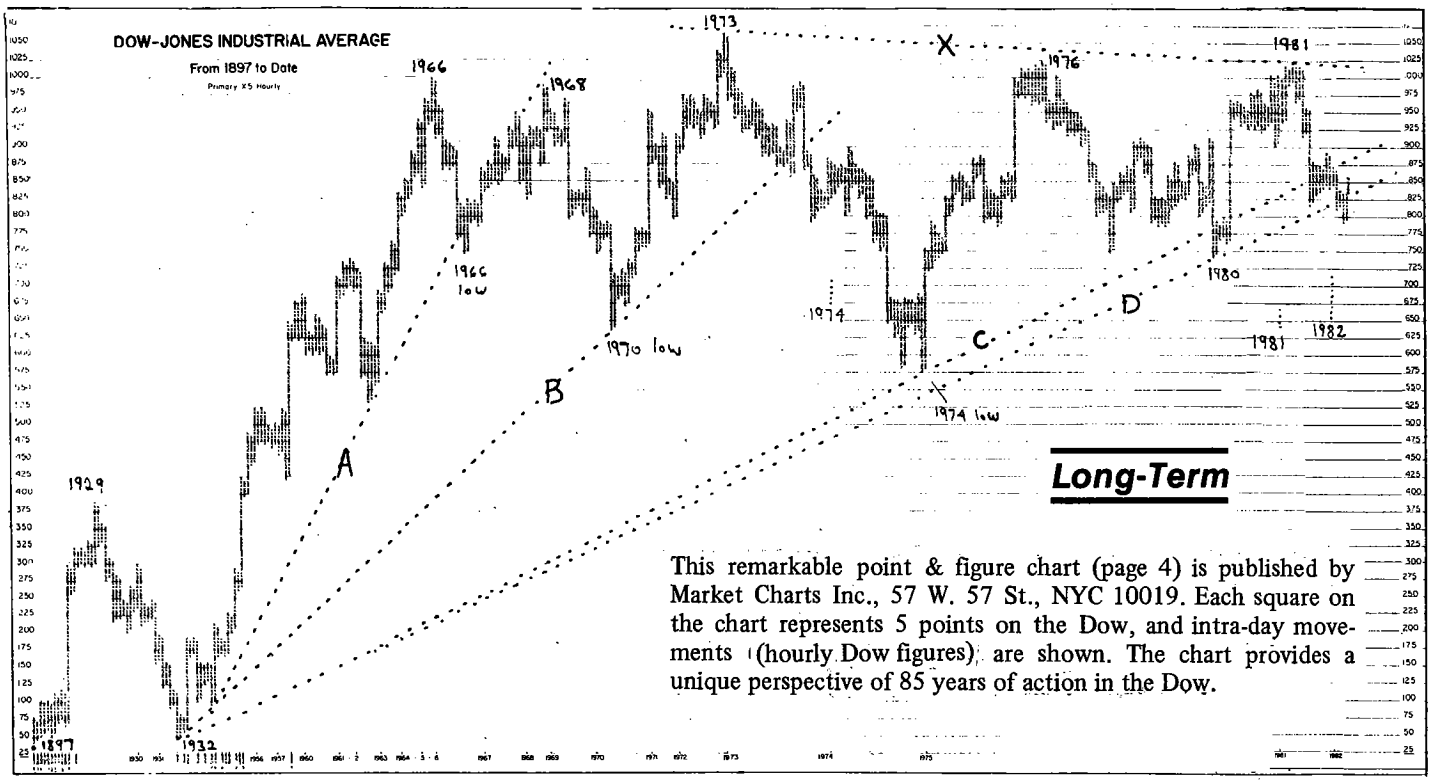
The class reunion (high school class of '42) was a great success. Out of 90 guys, 33 showed up (mostly with their second wives). Mostly, the fellows looked pretty good, but I have to admit that we looked a bit older than we did back in the 40's. We had cocktails and dinner, then each survivor told (briefly) what had happened since 1942. It was a tear jerker.

Everything had happened. Alcoholism, success, frustration, divorce, big money, fame, obscurity. We all loved it, from "Butch" Aufses, who is chief of surgery at Mt. Sinai Hospital to Jim Salter who graduated from West Point, was a fighter pilot in

Korea, then wrote four books and a few movies including Redford's classic "Downhill Racer."

The flight back to San Diego came all too soon. When the plane came in sight of the Pacific Ocean I murmured to myself, as I always do, "Welcome back to God's Country." I feel that way about the West, and I'm not embarrassed to say so. New York's the greatest city in the world, I was born there and I lived there until I was 35. But the West is where I moved to. I picked the West. I never want to live anyplace else.

PERSPECTIVE: Every once in a while I like to present a long-term market study, a study that may provide my readers with some idea of where we have been and where we could be going. I find this point and figure chart of the D-J Industrial Average of great interest. The chart traces the price action of the Dow from its inception in 1897–to the present.



This remarkable point & figure chart (page 4) is published by Market Charts Inc., 57 W. 57 St., NYC 10019. Each square on the chart represents 5 points on the Dow, and intra-day movements (hourly Dow figures) are shown. The chart provides a unique perspective of 85 years of action in the Dow.

I have analyzed the price action in terms of trendlines. The present era began from the extreme July, 1932 low of 41.22 on the Dow. From that low the Dow turned up into what was to be the greatest bull market in American history. The path of the bull market was delineated by trendline A, a trendline that connects the 1949 and 1962 bottoms. The great bull market ended on February 9, 1966 at Dow 995.15.

It is interesting to note the loss of momentum following the top. For 16 years following that top the Dow attempted to push appreciably above the 1000 level. Every effort failed.

From the 1966 high the Dow tumbled to an October 7, 1966 low of 744.32. From there a new rising trend materialized. The Dow "walked up" trendline A (but note that it dropped away from the trendline during 1968) and on December 3, 1968 the Dow topped out at 985.21. From this lofty peak the market slid off, then smashed to a 1970 low of Dow 631.16.

I have drawn a new trendline (B) connecting the 1932 and 1970 bottoms. After the 1970 low the Dow again advanced, and by January 11, 1973, the Dow had recorded a record high of 1051.50. But this high was fated to be followed by the worst bear market since 1929. By late 1974 the Dow had crashed to a low closing of 577.60.

A third trendline was drawn connecting the 1932 and 1974 lows (trendline C). From the 1974 base the Dow advanced again, and by 1976 the Dow had reached a peak of 1014.79. From the 1976 high a confused series of declines and feeble rallies took the Dow back to a 1980 low of 759.13. At the 1980 low the Dow violated the 49 year-old trendline C. This move constituted the third violation of the major trendline since the 1932 bottom.

I have drawn a fourth major trendline (D) connecting the 1932 and 1980 lows. From the 1980 low the Dow mounted a new advance. This rise carried the Dow to an April 27, 1981 peak of 1024.79. But no sooner had the Dow pushed above the 1000 level than the bear forces took over again. From the April, 1981 high the Dow started down. During September, 1981 the Dow cracked below trendline C.

A period of congestion followed during which the Dow clung to trendline C. But when the new year started (1982) the Dow turned weak again. By March of 1982 the Dow had fallen decisively below trendline D.

Where does the Dow stand now? Trendline D stands at approximately 840. In the past each of the major trendlines I have drawn have offered resistance. But once violated, the Dow fell considerably further. The single exception to this sequence was in 1980 when the Dow violated trendline C. Note that the Dow fell roughly another 35 points, then rallied to the 1981 high. Now again a long-term trendline has been violated–this time the violation entails trendline D.

To my mind it will be most important to see whether the Dow can mount an important advance from here. If it cannot, then the

Dow will in all probability drop away from trendline D on the downside. The next stop would be the 1980 low of 759.13. If that level does not hold, there would be nothing under the Dow until the 1974 low of 577.60.

I have drawn trendline X at the top of the chart connecting the 1973 and 1981 highs. This trendline has stopped every advance of the last 9 years. So we have the following picture: a trendline at the highs (X) which has halted all advances above 1000. And we have four bottom trendlines (A through D), none of which have held during market declines. Now the most recent trendlines (X and D) are converging. The tendency, so far, has been to the downside, and even now the Dow is clinging to the lower trendline. But we must be unbiased. Sooner or later (and probably sooner) the Dow must "make its decision." Another attack on trendline X–or a plunge to lower levels below trendline D. We should know which one before this year is out.

NOTES & QUOTES: In an historic armaments decision, the US recently decided to drop the venerable Colt 45 semi-automatic pistol in favor of a 9mm weapon (which would dovetail with NATO, which uses the 9mm). The Joint Service Small Arms Program tested most of the major 9mm weapons plus the Colt 45. Some of the conclusions: only the Beretta M92S and the Smith and Wesson M459 were reliable enough. But the Berretta was 10 times as reliable as the S & W. The Berretta, the Commision concluded, has no peer as a 9mm pistol and is easier to handle and more accurate than the Colt.

I concur. For fire power, accuracy, reliabilty, the Berretta 92S is hard to beat. The pistol holds 15 rounds, it's beautifully built, and outstandingly finished. During WW II I carried a Beretta 32 automatic in combat as a back up weapon and always swore by it. For home defense, the Beretta 92S is an outstanding weapon.

Speaking of weapons, people often ask me, "Russell, you read a thousand publications and talk to a lot of people. In your opinion, what's a good business to get in to?" I tell them, "Get into the business of killing. It's got an unlimited future, you've got the world to sell, and it's backed 1000% by your own government." You're surprised? Don't be, read this little UPI note.

WASHINGTON (UPI) — U.S. arms sales to other countries this year are likely to exceed $30 billion — more than any nation has sold in world history, a report said yesterday.

The old record, according to the figures compiled by the Center for Defense Information, was about $17 billion worth of weapons sold during the Ford administration in 1975.

The center, a privately funded non-partisan research group, said U.S. weapons exports for the fiscal year ending October 1982 easily will surpass those of the Soviet Union, which last year topped America in arms sales to the Third World.

It said the soaring arms sale figures are the result of a deliberate Reagan administration decision to reverse policies of the Carter administration, which had unsuccessfully tried to limit weapons sales to other countries.

The changes, the center added, include dropping an arbitrary ceiling on total arms sales, de-emphasizing human rights considerations on the part of the buying nations, ending the rule that barred introduction of advanced technology into regions of potential conflict, and ordering U.S. embassies to give help to American businessmen seeking to sell arms to other countries.

* *

San Diego is probably the most "out-doors" town in the US. Because of San Diegans love of the outdoors (the sun's out here about 325 days a year) the town is known as a poor movie town. The last time I saw people line up for a movie here was when the Godfather hit the screens. But now they're lining up for a new German film entitled "Das Boot" (the Boat). I saw the picture last week. My opinion–don't miss it! This unbelievably authentic film deals with the exploits and hardships of a Nazi U Boat crew during WW11. Let me put it this way: the movie is long, 2½ hours. But it went by like a 10 minute short. The audience left wrung-out, dazed, What a pic!

* *

This "recession" is digging DEEP. According to the Manufacturers Hanover report received today, "Even compared with depressed year-earlier levels, this year's estimated first quarter earnings performance was abysmal, skidding a huge 35% when measured on a year-over-year basis.....putting these results together (fourth and first quarters) brings the two-quarter earnings drop to a record $70 billion, paling by comparison its nearest rival for this dubious honor–the $35 billion, or 25%, decline in before-tax profits which occurred during the last two quarters of the 1973-75 recession."

* *

Sometimes I wonder how many billions of dollars have been lost (1) trying to beat inflation, and (2) trying to beat the market. Take the multi-billion dollar pension fund industry. As this newspaper clip states, the pension funds lost 3.3% last year, made 12% in 1979 and averaged a mere 7.7% over the last five years.

Remember, I've noted often that the average fund can just about average 10% over a 10 year period, and as you see the pension funds can't even do that. You might mull this over as you collect 12-13% on your risk-free T-bills. It may be a bit boring, "rolling over" those T-bills as they come due, but you're still doing better than most of the pro's.

Individually managed pension and profit-sharing funds posted an average return of 12% in 1979 and averaged 7.7% over the last five years, according to Hewitt Associates, an Illinois-based consulting firm on employee benefits and compensation. The stock market dragged down overall retirement fund investment results, with the average fund losing 3.3% in 1981, Hewitt reported, a loss slightly less than reflected in the market indexes.

* *

The "flat-rate" income tax is an idea whose time has come. But it's political dynamite. At 16% across the board, 16% of all corporate and individual income, the 1983 budget would be balanced. At 20% we could not only have no deficit but we could start paying off the national debt.

But think of it: with a simple 16% tax on all income we'd throw out of business the following: thousands of tax lawyers, thousands of accountants, thousands of lobbyists, thousands of tax shelter sellers. And perhaps the biggest problem of all is that with the flat-rate tax there would be no deductions for interest. What would happen to the building industry and all the other industries that depend on interest deductions. Of course, with no deficits interest rates would collapse.

As I said, the flat-rate tax is an idea whose time has come. Will it be tried? I think it will–when there's no other alternative and the nation is willing to put the monster income tax industry out of business.

* *

A few years ago I made a statement that drew a lot of comment from subscribers. I said that a man or woman who had $150,000 had less "right" to speculate than a person with only $10,000. The reason: at today's interest rates $150,000 or more is a living (it will bring you $350 a week at prevailing T-bills rates). But the person with $10,000 is entitled to be a bit more venturesome. He doesn't have as much at stake (actually, of course, the $10,000 should be considered "seed money" and should be used as the nucleus for building an estate.)

At any rate, I thought this news clip about a frugal Irishman underscored my statement. Conn, by the way, was probably the best light-heavyweight boxer who ever lived, and he very nearly beat the great Joe Louis (who was a heavy weight).

Former light-heavyweight champion Billy Conn, who twice fought Joe Louis for the heavyweight title, hasn't held a steady job since his retirement in 1948. But shed no tears for Billy.

Recently, he told columnist Ray Didinger of the Philadelphia Daily News: "I made $150,000 for the first Louis fight, $350,000 for the rematch. I took that money, bought myself a new Cadillac and put the rest in the bank. I'm still living off it today."

* *

What are the advantages of working for the government? Well, there are cost-of-living wages, great pensions, and it's hard to fire you. But perhaps the greatest benefit is that your group can get out of Social Security. And they're doing it, as this clip indicates!

WASHINGTON (AP) — The Social Security system, already in dire financial straits, is having to cope with a growing trend toward desertion by the only employers not legally bound to the plan — state and local governments (including several in San Diego) and non-profit organizations.

Health and Human Services Secretary Richard S. Schweiker said yesterday that many non-profit hospitals "are being swayed by ... private insurance organizations that promise protections similar to Social Security but at less cost."

I'm on the publishers' lists to receive just about every financial book that's published, and I look at the new ones carefully. I seldom read a book for "answers." Because books don't provide answers to individual investment problems. But good books do provide INFORMATION and IDEAS. Two new books are worth reading. One is Doug Casey's "Strategic Investing" , (Simon & Schuster), a most interesting book containing Doug's ideas on what's coming up in the 1980's and what you can do about it. His three-part scenarios of the coming disaster is alone worth the price of the book.

Most investors are ignorant of foreign investments and foreign markets. Adrian Day's "Investing Without Borders" (Alexandria House) provides all kinds of information of off-shore funds, foreign banks, international funds, etc. All in all, a most informative book.

SAN FRANCISCO: I've been cutting way down on my speaking, mainly because it's a lot of work, and I prefer putting the work into these Letters. But I'm going to reveal a secret. I'm an avid Cactus collector, and there's a little lady up San Francisco way who grows gorgeous Cacti, thousands of varieties. And I've been looking for an excuse to get up to see Annie Shein again. So when the people at Investment Seminars,Inc. asked me to speak in July at San Francisco, I said I'd be there. And I will.

It also sounds like a most interesting seminar. My friend, Bert Dohmen-Ramirez (Wellington Letter) will be speaking as will "Big Julie" Snyder (Moneyline), James Dines ("The original gold-bug"), Donald J. Hoppe (who writes a fine report), Montague Guild (LA money manager), Charles Allmon (of Growth Stock Outlook), and the man who originally gave me my start in this business, Barron's publisher, Robert Bleiberg.

The Conference will take place July 7-11 at the Fairmont Hotel. For full particulars on the conference call 800-327-8338 (in Florida call 305-672-0308).

LATE NOTES: It's never easy, readers, it's never easy. Short-term interest rates remain firm with the 91-day bills hitting yields of 12.65 today (aren't they supposed to be coming down?) The market has the put and call buyers both pulling their hair, with first a pop-up and then a quick drop. Nothing's clear yet, but it does seem as if this market is tired. The over-bought indicators stay over-bought, but Wall Street hangs on. The PTI is clinging to that trendline, and I want to see what kind of a pattern the PTI forms–and whether it can extend its advance from here.

GOLD: As my readers know, I am no longer bearish on gold. I think that there is a better than 50/50 chance that the 312.50 low was the final low. But I am also not optimistic about any big bull move in gold here. A lot of people are trading in and out of gold, they are playing silver against gold, they are hoping the English-Argentine war develops into a big, gold-popping epic conflict. I don't think gold is ready to do anything important, and I don't think the English and the Argentines are about to set off World War III.

If you're holding a little gold for "emergency purposes," well hang on. I have a little cluster of gold coins that I'll hold until hell freezes over. Besides, I like to be able to show my kids what real, honest, non-manipulatable money looks like.

But as for a new bull move in gold, I think we've got to wait. A bull market may have started for gold at 312.50, but we won't know it for a while. And in the meantime, it's expensive to hold large quantities of gold while waiting for a disaster. (The 50-week moving average for gold is now 405, while the 13-week MA is 353. The 5-week MA is 350). Relax.

NEXT MAILING: May 19, 1982